No. 257.

Supreme Court of the United States,

Brief of Paige for Compl't.

OCTOBER TERM, 1898.

Filed April 8, 1899.

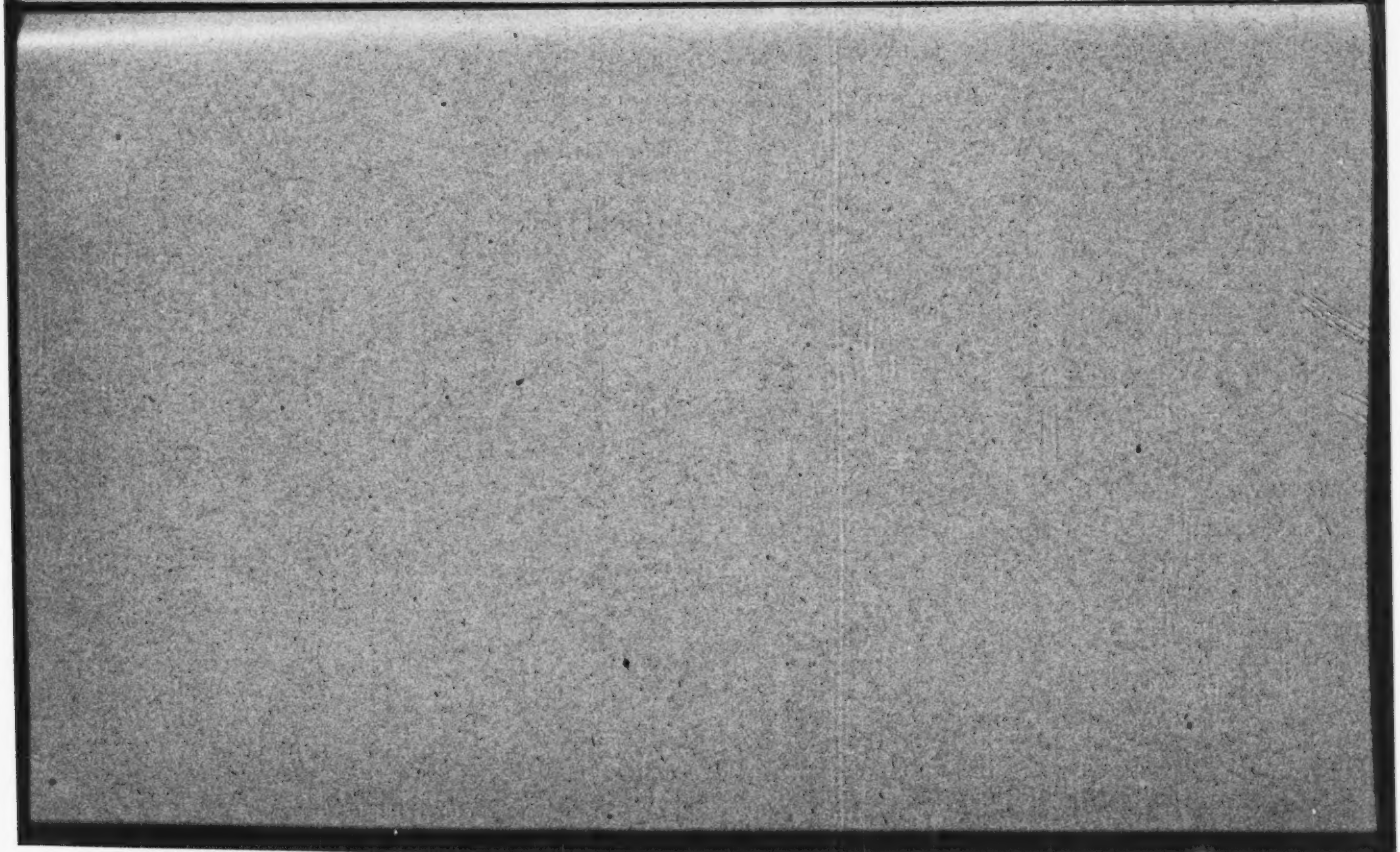
NUMBER TWO HUNDRED AND [illegible]

KENT K. HAYDEN,

against

GEORGE G. WILLIAMS AND JOHN B. DODD.

BRIEF FOR COMPLAINANT.



Supreme Court of the United States.

OCTOBER TERM, 1898.

NUMBER TWO HUNDRED AND FIFTY-SEVEN.

KENT K. HAYDEN, as receiver,

against

GEORGE G. WILLIAMS and JOHN B. DODD.

BRIEF FOR COMPLAINANT.

Abstract or Statement of Case.

FIRST HEAD: *Nature and Condition of the Action.*

The action is in equity—a bill exhibited by the receiver of the concerns of the Capital National Bank of Lincoln, Nebraska, to recover of the respondents, who are all of the stockholders of that bank resident in New York (R. 19), dividends which had been paid to them out of the capital of the bank.

In the circuit court the complainant had a decree.

On appeal to the circuit court of appeals for the second circuit that court has certified two questions.

SECOND HEAD: *The Certificate.*

(R. 1.) **"Statement of Facts.**

"The complainant is the receiver of the Capital National "Bank of Lincoln, Nebraska, which suspended payment "in January, 1893, in a condition of hopeless insol- "vency. The stockholders, including the defendants, "have been assessed to the full value of their respective "holdings, but the money thus obtained, added to the

" amount realised from the assets, would not be sufficient, " even if all dividends paid during the bank's existence " were repaid to the receiver, to pay 75% of the claims of " the bank's creditors. This suit was brought to compel " the repayment of and accounting for certain dividends " paid by the bank to the defendants, as holders of capital " stock of the bank of the par value of $5,000, on the " ground alleged in the bill, that each of said dividends " was fraudulently declared and paid out of the capital " of the bank and not out of net profits. A similar suit " was brought against the stockholders resident in Ne- " braska, and upon appeal from a decree on demurrers " was sustained by the circuit court of appeals in the " eighth circuit, defendants in that case conceding by " their demurrers that the bank was insolvent when each " dividend was paid.

" The bank was organised in 1883, with a capital of " $100,000, which was increased to $200,000 June 2, 1884, " and to $300,000 July 21, 1886. The dividends which " were paid from time to time were as follows:

" DATE.	AMOUNT PAID IN DIVIDENDS.	DEFENDANT RECEIVED.
" 1885, Jan. 13..	$15,000	$187.50
" " July 14..	13,000	162.50
" 1886, Jan. 12..	16,000	200.00
" " July 13..	14,000	175.00
" 1887, Jan. 11..	18,000	300.00
" 1887, July 12..	18,000	300.00
" 1888, Jan. 10..	18,000	300.00
" " July 10..	18,000	300.00
" 1889, Jan. 8..	18,000	300.00
" " July 9..	18,000	300.00
" 1890, Jan. 14..	15,000	250.00
" " July 11..	15,000	250.00
" 1891, Jan. 13..	15,000	250.00
" " July 13..	15,000	250.00
" 1892, Jan. 12..	15,000	250.00
" " July 12..	12,000	200.00

" All dividends except the last were paid to the de-
" fendant Williams, a stockholder to the amount of
" $5,000 from the organization of the bank. The last
" dividend was paid to defendant Dodd, who bought
" Williams' stock and had the same transferred to his
" own name December 16, 1891.

" When the dividend of Jan. 6, 1889, was declared and
" paid, and when each subsequent dividend down to and
" including July, 1891, was declared and paid, there were
" no net profits, the capital of the bank was impaired,
" and the dividends were paid out of capital, but the bank
" was still solvent.

" When the dividends of January and July, 1892, were
" declared and paid, there were no net profits, the capital
" of the bank was lost, and the bank actually insolvent.

" The defendants, neither of whom was an officer or
" director, were ignorant of the financial condition of the
" bank, and received the dividends in good faith, relying
" on the officers of the bank and believing the dividends
" were coming out of profits.

" *Questions Certified.*

" Upon the facts set forth, the questions of law, concern-
" ing which this court desires the instruction of the Su-
" preme Court for its proper decision, *is:*

" Can the receiver of a national bank recover a dividend
" paid not at all out of profits, but entirely out of capital,
" when the stockholder receiving such dividend acted in
" entire good faith, believing the same to be paid out of
" profits, and when the bank at the time such dividend
" was declared and paid was not insolvent?

" Has a U. S. circuit court jurisdiction to entertain a bill
" in equity brought by the receiver of a national bank
" against stockholders to recover dividends which it is
" claimed were improperly paid when such suit is brought
" against two or more stockholders and embraces two or

"more dividends, and when the objection that there is an "adequate remedy at law is raised by the answer?" (R. 1–3.)

Acts of Congress.

Sections 5199 and 5204 of the Revised Statutes are as follows:

"SEC. 5199. The directors of any association may, "semi-annually, declare a dividend of so much of the net "profits of the association as they shall judge expedient; "but each association shall, before the declaration of a "dividend, carry one-tenth part of its net profits of the "preceding half-year to its surplus fund until the same "shall amount to twenty per centum of its capital stock."

"SEC. 5204. No association, or any member thereof, "shall, during the time it shall continue its banking oper- "ations, withdraw, or permit to be withdrawn, either in "the form of dividends or otherwise, any portion of its "capital. If losses have at any time been sustained by "any such association, equal to or exceeding its undivided "profits then on hand, no dividend shall be made; and "no dividend shall ever be made by any association, while "it continues its banking operations, to an amount greater "than its net profits then on hand, deducting therefrom "its losses and bad debts. All debts due to any associa- "tions, on which interest is past due and unpaid for a "period of six months, unless the same are well secured, "and in process of collection, shall be considered bad "debts within the meaning of this section. But nothing "in this section shall prevent the reduction of the capital "stock of the association under section fifty-one hundred "and forty-three."

Other provisions relating to capital and dividends are as follows:

"SEC. 5140. At least fifty per centum of the capital

"stock of every association shall be paid in before it shall "be authorized to commence business; and the remainder "of the capital stock of such association shall be paid in "installments of at least ten per centum each, on the "whole amount of the capital, as frequently as one in- "stallment at the end of each successive month from the "time it shall be authorized by the Comptroller of the "Currency to commence business; and the payment of "each installment shall be certified to the Comptroller, "under oath, by the president or cashier of the associa- "tion.

"SEC. 5141. Whenever any shareholder, or his as- "signee, fails to pay any installment on the stock when "the same is required by the preceding section to be paid, "the directors of such association may sell the stock of "such delinquent shareholder at public auction, having "given three weeks public notice thereof in a newspaper "published and of general circulation in the city or "county where the association is located, or if no news- "paper is published in said city or county, then in a news- "paper published nearest thereto, to any person who will "pay the highest price therefor, to be not less than the "amount then due thereon, with the expenses of adver- "tisement and sale; and the excess, if any, shall be paid "to the delinquent shareholder. If no bidder can be "found who will pay for such stock the amount due "thereon to the association, and the cost of advertise- "ment and sale, the amount previously paid shall be for- "feited to the association, and such stock shall be sold "as the directors may order, within six months from the "time of such forfeiture, and if not sold it shall be can- "celled and deducted from the capital stock of the asso- "ciation. If any such cancellation and reduction shall "reduce the capital of the association below the minimum "of capital required by law, the capital stock shall,

"within thirty days from the date of such cancellation, "be increased to the required amount; in default of "which a receiver may be appointed, according to the pro- "visions of section fifty-two hundred and thirty-four, to "close up the business of the association."

"SEC. 5151. The shareholders of every national bank- "ing association shall be held individually responsible, "equally and ratably, and not one for another, for all con- "tracts, debts, and engagements of such association, to the "extent of the amount of their stock therein, at the par "value thereof, in addition to the amount invested in such "shares; except that shareholders of any banking associa- "tion now existing under State laws, having not less than "five millions of dollars of capital actually paid in, and a "surplus of twenty per centum on hand, both to be de- "termined by the Comptroller of the Currency, shall be "liable only to the amount invested in their shares; and "such surplus of twenty per centum shall be kept undi- "minished, and be in addition to the surplus provided for "in this Title; and if at any time there is a deficiency in "such surplus of twenty per centum, such association "shall not pay any dividends to its shareholders until the "deficiency is made good, and in case of such deficiency, "the Comptroller of the Currency may compel the associ- "ation to close its business and wind up its affairs under "the provisions of Chapter four of this Title.

"SEC. 5207. No association shall hereafter offer or re- "ceive United States notes or national bank notes as secu- "rity or as collateral security for any loan of money, or for "a consideration agree to withhold the same from use, or "offer or receive the custody or promise of custody of such "notes as security, or as collateral security, or considera- "tion for any loan of money. Any association offending "against the provisions of this section shall be deemed

"guilty of a misdemeanor, and shall be fined not more "than one thousand dollars and a further sum equal to "one-third of the money so loaned. The officer or officers "of any association who shall make any such loan shall "be liable for a further sum equal to one-quarter of the "money loaned; and any fine or penalty incurred by a "violation of this section shall be recoverable for the bene- "fit of the party bringing such suit.

"SEC. 5208. It shall be unlawful for any officer, clerk, "or agent of any national banking association to certify "any check drawn upon the association unless the person "or company drawing the check has on deposit with the "association, at the time such check is certified, an amount "of money equal to the amount specified in such check. "Any check so certified by duly authorized officers shall "be a good and valid obligation against the association; "but the act of any officer, clerk, or agent of any associa- "tion, in violation of this section, shall subject such "bank to the liabilities and proceedings on the part of "the Comptroller as provided for in section fifty-two hun- "dred and thirty-four.

"SEC. 5209. Every president, director, cashier, teller, "clerk, or agent of any association, who embezzles, "abstracts, or wilfully misapplies any of the moneys, "funds, or credits of the association; or who, without "authority from the directors, issues or puts in circula- "tion any of the notes of the association; or who, with- "out such authority, issues or puts forth any certificate "of deposit, draws any order or bill of exchange, makes "any acceptance, assigns any note, bond, draft, bill of "exchange, mortgage, judgment, or decree; or who makes "any false entry in any book, report, or statement of the "association, with intent, in either case, to injure or defraud "the association or any other company, body politic or

"corporate, or any individual person, or to deceive any "officer of the association, or any agent appointed to ex- "amine the affairs of any such association; and every "person who with like intent aids or abets any officer, "clerk, or agent in any violation of this action, shall be "deemed guilty of a misdemeanor, and shall be im- "prisoned not less than five years nor more than ten."

BRIEF OF THE ARGUMENT.

I.

The capital of a national bank is a trust fund for the security of the creditors and can be followed into the hands of any volunteer.

1. *This is settled by the adjudged cases:*

In *Curran* v. *Arkansas*, 15 How. 304, the Court, speaking by Mr. Justice Curtis, said:

(p. 307.) "The plaintiff is a creditor of an insolvent "banking corporation. The assets of such a corporation "are a fund for the payment of its debts. If they are "held by the corporation itself, and so invested as to be "subject to legal process, they may be levied on by such "process. *If they have been distributed among stock-* "*holders*, or gone into the hands of others than *bona fide* "creditors or purchasers, *leaving debts of the corporation* "*unpaid, such holders take the property charged with* "*the trust in favor of creditors, which a court of equity* "*will enforce, and compel the application of the prop-* "*erty to the satisfaction of their debts.*

"This has been often decided, and rests upon plain "principles. In 2 Story's Eq. Jur. § 1252, it is said, "'Perhaps, to this same head of implied trusts upon pre-

" ' sumed intention, (although it might equally well be
" ' deemed to fall under the head of implied trusts by
" ' operation of law,) we may refer that class of cases
" ' where the stock and other property of private corpora-
" ' tions is deemed a trust fund for the payment of the
" ' debts of the corporation; so that the creditors have a
" ' lien, or right of priority of payment on it, in prefer-
" ' ence to any of the stockholders of the corporation.'
" Thus, for example: ' *The capital stock of an incorpor-*
" ' *ated bank is deemed a trust fund for all the debts of*
" ' *the corporation: and no stockholder can entitle him-*
" ' *self to any dividend or share of such capital stock,*
" ' *until all the debts are paid, and if the capital stock*
" ' *should be divided, leaving any debts unpaid, every*
" ' *stockholder, receiving his share of the capital stock,*
" ' *would, in equity, be held liable* pro rata *to contribute*
" ' *to the discharge of such debts out of the fund in his*
" ' *own hands.*' In conformity with this is the doctrine
" held by this court in Mumma *v.* The Potomac Com-
" pany, 8 Peters, 281.

" The cases of Wood *v.* Dummer, 3 Mason, 308;
" Wright *v.* Petrie, 1 Smedes & Marsh. 319; Nevitt *v.*
" Bank of Port Gibson, 6 Id., 513; Hightower *v.* Thorn-
" ton et al. 8 Georgia R. 493; Nathan *v.* Whitlock, 3
" Edwards, C. R. 215, affirmed by the chancellor, (9
" Paige, 152,) contain elaborate examinations of this
" doctrine, and it has been affirmed and applied in many
" other cases";

And at page 311, " Whatever technical difficulties exist
" in maintaining an action at law by or against a corpora-
" tion after its charter has been repealed, *in the appre-*
" *hension of a court of equity, there is no difficulty in a*
" *creditor following the property of the corporation into*
" *the hands of anyone not a* bona fide *creditor or pur-*
" *chaser, and asserting his lien thereon, and obtaining*

"*satisfaction of his just debt out of that fund specif-*
"*ically set apart for its payment when the debt was con-*
"*tracted, and charged with a trust for all the creditors*
"*when in the hands of the corporation;* which trust the
"repeal of the charter does not destroy. Chancellor Kent,
"in 2 Com. 307, n., says, 'The rule of the common law
"'has in fact become obsolete. It has never been applied
"'to insolvent or dissolved moneyed corporations in Eng-
"'land. The sound doctrine now is, as shown by statutes
"'and judicial decisions, that the capital and debts of bank-
"'ing and other moneyed corporations, constitute a trust
"'fund and pledge for the payment of creditors and stock-
"'holders, and a court of equity will lay hold of the fund
"'and see that it be duly collected and applied.' The
"case of Hightower *v.* Thornton, 8 Georgia R. 491, and
"other cases before referred to in this opinion, are in con-
"formity with this doctrine";

And at page 315, "Whatever losses a bank sustains,
"are losses of the capital paid in by its stockholders;
"that is the only fund it has to lose. When it has be-
"come insolvent, it has lost all that fund, and has noth-
"ing belonging to its stockholders. In some sense a bank
"may be said to be indebted to its stockholders for the
"capital they have paid in. With the leave of the State,
"they have a right to withdraw it, *after all debts are*
"*paid*, and if the State is itself the sole stockholder, it
"may withdraw its capital while any of it shall remain.
"But, from the very nature of things, it cannot withdraw
"capital from an insolvent bank, because it has none of
"their capital remaining. When insolvent, its assets
"belong solely to its creditors."

Italics mine.

In *Railroad Company* v. *Howard*, 7 *Wall*, 392, the Court, speaking by Mr. Justice Clifford, said (p. 410):

"Moneys derived from the sale and transfer of the

" franchises and capital stock of an incorporated company " are assets of the corporation, *and as such constitute a* " *fund for the payment of its debts*, and if held by the " corporation itself, and so invested as to be subject to " legal process, the fund may be levied on by such pro- " cess; *but if the fund has been distributed among the* " *stockholders*, or passed into the hands of other than " *bona-fide* creditors or purchasers, *leaving any debts of* " *the corporation unpaid, the established rule in equity* " *is that such holders take the fund charged with the* " *trust in favor of creditors, which a court of equity* " *will enforce, and compel the application of the same* " *to the satisfaction of their debts.*—Story's Equity " Jurisprudence (9th ed.), § 1252; Mumma *v.* Potomac " Company, 8 Peters, 286; Wood *v.* Dummer, 3 Mason, " 308; Vose *v.* Grant, 15 Massachusetts, 522; Spear *v.* " Grant, 16 Massachusetts, 14; Curran *v.* Arkansas, 15 " Howard, 307.

" Regarded as the trustee of the corporate fund, the " corporation is bound to administer the same in good " faith for the benefit of creditors and stockholders, and " all others interested in its pecuniary affairs, and *any-* " *one receiving any portion of the fund by volun-* " *tary transfer, or without consideration, may be* " *compelled to account to those for whose use the fund* " *is held. Creditors are preferred to stockholders on* " *account of* THE PECULIAR TRUST *in their favor, and* " *because the latter, as constituent members of the cor-* " *porate body, are regarded as sustaining, in that aspect,* " *the same relation to the former as that sustained by the* " *corporation.*"

This language was repeated by the Court in *Scammon* v. *Kimball*, 92 U. S., 362, 367.

In *Sanger* v. *Hoag*, 17 Wall, 610, the Court, speaking by Mr Justice Miller, said (p. 620):

" Though it be a doctrine of modern date, we think it " now well established that the capital stock of a corpora- " tion, especially its unpaid subscriptions, is a trust fund " for the benefit of the general creditors of the corpora- " tion."

In *Barings* v. *Dabney*, 19 Wall, 1, the Court, speaking by Mr. Justice Bradley, said (p. 9):

" It was expressly decided, in *Curran* v. *The State of* " *Arkansas*, 15 Howard, 304, *that if the capital of a State* " *bank, like the one in question, be withdrawn by the* " *State*, either for the payment of its own debts or for " deposit in the State Treasury, *it is a violation of the* " *pledges by which the capital of the bank*, though de- " rived from State resources or State obligations, *was set* " *apart and appropriated as the basis of the inde-* " *pendent credit of the bank;* and that a law passed to " effect such a withdrawal or misappropriation impaired " the validity of the contracts held by the creditors of the " bank."

In *Sanger* v. *Upton*, 91 U. S., 56, the Court, speaking by Mr. Justice Swayne, said (p. 60):

" The capital stock of an incorporated company is a " fund set apart for the payment of its debts. It is a " substitute for the personal liability which subsists in " private co-partnerships. When debts are incurred, a " contract arises with the creditors that it shall not be " withdrawn or applied, otherwise than upon their de- " mands, until such demands are satisfied. *The creditors* " *have a lien upon it in equity. If diverted, they may* " *follow it as far as it can be traced, and subject it to* " *the payment of their claims*, except as against holders " who have taken it *bona fide* for a valuable consideration " and without notice. *It is publicly pledged to those* " *who deal with the corporation for their security.*"

In *Finn* v. *Brown*, 142 U. S., 56, the Court sustained the recovery of a dividend, but in that case the bank was insolvent when the dividend was declared and paid, and the holding therefore does not come within the question certified.

In *Vose* v. *Grant*, 15 Mass. 505, and *Spear* v. *Grant*, 16 Mass. 9, cited by Mr. Justice Clifford in *Railroad Company* v. *Howard*, 7 Wall. 392, 410, the bank was not insolvent.

In *Bartlett* v. *Drew*, 57 N. Y., 587, and *Hastings* v. *Drew*, 76 N. Y., 9, the corporation, which was a steamboat company, sold three steamboats and divided the proceeds among its stockholders. It was not insolvent. On the contrary the complaint alleged that it, until "the distribution of its capital stock and assets as "hereinafter set forth, was possessed of and owned capi- "tal stock and assets, more than sufficient for the pay- "ment of all its debts and liabilities" (Appeal Book, fol. 10, Ct. App. Cases, Bar Association, Vol. 5 of 1874).

And the court in *Bartlett* v. *Drew*, 57 N. Y., 587, speaking by Mr. Commissioner Reynolds, said (p. 589):

"The circumstance that the debtor is a foreign corpo- "ration, or that the defendant, Drew, was its president, "director or stockholder, is quite immaterial, if it be "found that Drew has any of the assets or property of "the corporation which ought to be applied in payment "of its debts. It is equally immaterial, whether he got it "by fair agreement with his associates, or by any wrong- "ful act. If the law dooms it to the payment of the "debts of the corporation, it may be taken in some form "by the creditor. It is a very plain proposition that the "the stock and property of every corporation is to be re- "garded as a trust fund for the payment of its debts, and "its creditors have a lien and the right to priority of

" payment over any stockholder, (2 Story Eq. Jur., § " 1252.)"

And at page 590: "As before suggested, it does not " matter how it came to the possession of the defendant, " Drew. It is enough that he had it, and it was so much " of the assets of the corporation as ought to be devoted " to the payment of the debts of the company, and " his claim as a stockholder could not prevail over the " creditor's prior right. (*Curran* v. *State of Arkansas*, " 15 How [U. S.,] 305; *Tinkham* v. *Borst*, 31 Barb., 407, " 412; 2 Kent Com., 307; 2 Story's Eq. Jur., §1252)."

Hayden v. *Thompson*, 36 U. S. App., 361. This is the case decided by the court of appeals of the eighth circuit, spoken of in the certificate (R. 1).

Of course, this is quite different from *Hollins* v. *Brierfield Coal and Iron Company*, 150 U. S., 371. The receiver has all the powers and all the rights of all the creditors put together, if they were all here, each with a judgment and execution returned unsatisfied and a creditor's bill filed. If *Hollins*, in that case, had had the sort of lien necessary for that sort of action upon *any* assets, not capital necessarily, the decision would have been otherwise. In this case, the question certified assumes that complainant had the sort of interest necessary for this sort of action in *assets* though not in *capital*, and *Finn* vs. *Brown*, 142 U. S., 156, so holds.

There is not anything in the *Hollins case* which is inconsistent with this. In that case the Court, speaking by Mr. Justice Brewer, said (150 U. S., 371, 383): "With " reference to the suggestion in this last paragraph, it " may be observed that the court does not attempt to de- " termine who are proper parties to maintain a suit for " the administration of the assets of an insolvent corpora- " tion. All that it decides is, that when a court of equity " does take into its possession the assets of an insolvent

"corporation, it will administer them on the theory that "they in equity belong to the creditors and stockholders "rather than to the corporation itself. In other words, "and that is the idea which underlies all these expres- "sions in reference to 'trust' in connection with the "property of a corporation, the corporation is an entity, "distinct from its stockholders as from its creditors. "Solvent, it holds its property as an individual holds his, "free from the touch of a creditor who has acquired no "lien; free also from the touch of a stockholder who, "though equitably interested in, has no legal right to, "the property. Becoming insolvent, the equitable in- "terest of the stockholders in the property, together with "their conditional liability to the creditors, place the "property in a condition of trust, first, for the creditors, "and then for the stockholders. Whatever of trust there "is arises from the peculiar and diverse equitable rights "of the stockholders as against the corporation in its "prosperity and their conditional liability to its credi- "tors. It is rather a trust in the administration of the "assets after possession by a court of equity than a trust "attaching to the property as such, for the direct benefit "of either creditor or stockholder.

"Again, in the case of the *Wabash, St. Louis & Pacific* "*Railway* v. *Ham*, 114 U. S. 587, it appeared that four "railway corporations, owing debts, were consolidated "under authority of law, and, by the terms of the con- "solidation agreement, the new corporation was to protect "the debts of the old. Subsequently, the new corpora- "tion executed a mortgage on all its property, and in a "contest between the mortgagees and the unsecured cred- "itors of one of the constituent companies, the court held "that the lien of the mortgagees was prior. In respect "to this, Mr. Justice Gray (p. 594) thus stated the law: "'It was contended that the property of the Toledo and

" ' Wabash Railway Company was a trust fund for all its
" ' creditors, and that upon the consolidation, the Toledo,
" ' Wabash and Western Railway Company took the
" ' property of the Toledo and Wabash Railway Company
" ' charged with the payment of all its debts. The prop-
" ' erty of a corporation is doubtless a trust fund for the
" ' payment of its debts, in the sense, that when a corpor-
" ' ation is lawfully dissolved and all its business wound
" ' up, or when it is insolvent, all its creditors are enti-
" ' tled in equity to have their debts paid out of the cor-
" ' porate property before any distribution thereof among
" ' the stockholders. It is also true, in the case of a cor-
" ' poration, as in that of a natural person, that any con-
" ' veyance of property of the debtor, without authority
" ' of law, and in fraud of existing creditors, is void as
" ' against them.'

" The case of *Fogg* v. *Blair*, 133 U. S. 534, 541, pre-
" sented a similar question, and this court by Mr. Justice
" Field, observed: ' We do not question the general doc-
" ' trine invoked by the appellant, that the property of a
" ' railroad company is a trust fund for the payment of its
" ' debts, but do not perceive any place for its application
" ' here. That doctrine only means that the property
" ' must first be appropriated to the payment of the debts
" ' of the company before any portion of it can be distrib-
" ' uted to the stockholders; it does not mean that the
" ' property is so affected by the indebtedness of the com-
" ' pany that it cannot be sold, transferred or mortgaged
" ' to *bona fide* purchasers for a valuable consideration,
" ' except subject to the liability of being appropriated
" ' to pay that indebtedness. Such a doctrine has no
" ' existence.'

" In the case of *Hawkins* v. *Glenn*, 131 U. S., 319, 332,
" which was an action brought by the trustee of a cor-
" poration against certain of its stockholders to recover

" unpaid subscriptions, and in which the defence of the " statute of limitations was pleaded, Chief Justice Fuller " referred to this matter in these words: 'Unpaid sub- " 'scriptions are assets, but have frequently been treated " 'by courts of equity as if impressed with a trust *sub* " '*modo*, upon the view that, the corporation being insol- " 'vent, the existence of creditors subjects these liabilities " 'to the rules applicable to funds to be accounted for as " 'held in trust, and that, therefore, statutes of limitation " 'do not commence to run in respect to them until the " 'retention of the money has become adverse by a refusal " 'to pay upon due requisition.'

" These cases negative the idea of any direct trust or " lien attaching to the property of a corporation in favor " of its creditors, and at the same time are entirely con- " sistent with those cases in which the assets of a cor- " poration are spoken of as a trust fund, using the term " in the sense that we have said it was used.

" The same idea of equitable lien and trust exists to " some extent in the case of partnership property. " Whenever, a partnership becoming insolvent, a court of " equity takes possession of its property, it recognizes the " fact that in equity the partnership creditors have a right " to payment out of those funds in preference to in- " dividual creditors, as well as superior to any claims of " the partners themselves. And the partnership property " is, therefore, sometimes said, not inaptly, to be held in " trust for the partnership creditors, or that they have an " equitable lien on such property. Yet, all that is meant " by such expressions is the existence of an equitable " right which will be enforced whenever a court of equity, " at the instance of a proper party and in a proper pro- " ceeding, has taken possession of the assets. It is never " understood that there is a specific lien, or a direct trust.

" A party may deal with a corporation in respect to its

"property in the same manner as with an individual "owner, and with no greater danger of being held to have "received into his possession property burdened with a "trust or lien. The officers of a corporation act in a "fiduciary capacity in respect to its property in their "hands, and may be called to an account for fraud or "sometimes even mere mismanagement in respect thereto; "but as between itself and its creditors the corporation is "simply a debtor, and does not hold its property in trust, "or subject to a lien in their favor, in any other sense "than does an individual debtor. That is certainly the "general rule, and if there be any exceptions thereto they "are not presented by any of the facts in this case. "Neither the insolvency of the corporation, nor the exe-"cution of an illegal trust deed, nor the failure to collect "in full all stock subscriptions, nor, all together, gave to "these simple contract creditors any lien upon the prop-"erty of the corporation, nor charged any direct trust "thereon."

There is this difference between a bank and a human being. The latter has no stockholders. He is a single, simple, being. If he has any money he keeps it as he pleases; if he do so choose, partly in his right-hand pocket, partly in his left-hand pocket, partly in his drawer, partly in his safe, partly in his bank, and partly, it may be, he buries in the ground. But a bank has stockholders —and if its directors commit any of its money to its stockholders, that money being the money of the bank and not of the stockholders, why are those stockholders any other than the pockets, the drawer, the safe, the bank and the hiding-place of the human being?

Nobody has ever pretended that the "trust" or the "lien" is good against anybody but a volunteer.

I do, however, claim this for the "trust," which could not be claimed against an human being. An human being, being solvent, *can give away his property*. I submit that a bank *cannot give* away any of its property, though it be perfectly solvent and though the giving away of the property does not make it insolvent. To that extent, I submit, the "trust" is *good*.

2. *The same result will be reached by reasoning from the rule that a dividend paid*, when the bank is insolvent, *can be recovered back*.

In *Finn* v. *Brown*, 142 U. S. 56, there were transferred to defendant, who had been a director and the vice-president of the bank, for about a month, fifty shares of stock from the stock of the president, and a dividend of twenty-five per cent. was made and $1,250 was put to the credit of the defendant as the owner of that stock. The defendant testified, that as soon as he was told of the transactions he repudiated the whole of them and gave a cheque for the $1,250, *not to the bank but to the president, and that he knew nothing about the condition of the bank and so far from thinking it to be insolvent he supposed it to be in flourishing circumstances*. The Court evidently believed him, as will appear from what is to be quoted from the opinion. At any rate what he testified to must have been taken as true, as the trial court refused to let him go to the jury. The defendant really owned twenty shares upon which he received $500, making a dividend of $1,750 in all. The Court, speaking by Mr. Justice Blatchford, said (p. 70): "In regard to the dividend of 25 per cent. "it was clearly fraudulent and unlawful. The defendant "did not get rid of his liability for the $1,250 by draw- "ing his check for that sum in favor of DeWalt (the presi-

"dent) individually and handing the same to DeWalt. "The money belonged to the bank, and ought to have been "restored to the bank. The dividend being unlawful, and "the $1,250 having been paid to the defendant by the "bank, by being transferred to his credit by the bank on "its books, it was not for him to take the place of the "bank and to pay the money to DeWalt."

And at page 71: "The jury would not have been justi- "fied in holding the defendant not liable for the assess- "ment on the 50 shares or for the $1,750 dividend. The "dividend was undoubtedly fraudulent, and the records of "the bank were falsified in showing that the defendant "was present at the meeting at which the dividend was "declared. It was declared, probably, by DeWalt him- "self alone, for the purpose of showing a fictitious pros- "perity and of concealing from the public and the direc- "tors the real condition of the affairs of the bank. The "defendant had no previous connection with banking "business, and was deceived by DeWalt. But all this "cannot relieve him from liability."

The Court thus held that a dividend declared and paid when the bank was insolvent could be recovered back. In that case, of course, the dividend was not paid out of capital, because there was not any capital to pay it out of. The capital was all gone.

But if the assets of a bank are impressed with a trust in favor of its creditors when it is insolvent, they must be impressed with the same trust when it is solvent. The mere fact that the value of the assets of a corporation has sunk below the amount of its debts, although as yet unknown to anybody cannot possibly *make a new contract* between the corporation and its *then* creditors.

It will be observed that the question certified does not refer to a time fixed by an *act* of insolvency, but to a time fixed by the *fact* of insolvency:—The court of appeals

evidently being of the opinion that the *mere fact* of insolvency made it possible to recover back a dividend declared and paid when the bank was in that condition.

But if the assets of the bank had not already been impressed with a trust in favor of the creditors, by what act of what parties, or by the meeting of whose minds, or by what statute, or by what rule of presumed intention, *did they become so at the instant when the value of the assets fell one cent below the amount of the debts:* that condition of things being unknown to anybody at the time, but discovered afterwards?

Of course there was never any such act of any parties—no minds ever met on any such proposition—no statute ever existed so providing and there never was any such rule of presumed intention, *and it follows* that if the assets of a bank are impressed with a trust in favor of its creditors where it is insolvent, *they must have* ALWAYS *been impressed with such a trust.*

II.

The Statutes of the United States make the payment of a dividend out of capital illegal and *ultra vires* of the corporation. Money thus paid, therefore, still remains the property of the corporation and can be followed into the hands of any volunteer.

I. *The Statutes of the United States make the payment of a dividend out of capital illegal and* ultra vires.

"When Congress made provision for a system of national "banks, it undertook at the same time to make provision

"for the security of those dealing with such banks. By "requiring the deposit with the Treasurer of the United "States of U. S. Registered bonds which may at the proper "time be sold under the direction of the Comptroller of the "Currency a special fund was provided for the redemption "of the circulating notes of the bank. To provide for any "deficit in the event of insolvency each shareholder was "required to respond to the full extent of his holding, in "addition to the full-paid par value of his shares, whenever "an assessment to pay the debts of the association might "become necessary. (Sec. 5151, 5234.) Congress further "provided, and provided most carefully, for the preserva- "tion of the capital of the bank intact. The amount of the "nominal capital of each bank is of course known to or easily "ascertainable by whomever deals with it as depositor "or otherwise. If the nominal capital is at all times repre- "sented by free assets in the bank's hands, there is reason- "able assurance to those dealing or about to deal with the "bank that they may do so with safety. That such a fund "should be created, and kept at all times intact as a reserve "fund upon the continued existence of which depositors "and persons dealing with the bank could rely, was ex- "pressly, and in the most careful and peremptory language "required by the statute. The provisions for the creation "and preservation of this fund are found in the following "sections. Sections 5140 and 5141 provide for payment in "of the capital, fifty per cent. before the association shall "be authorized to commence business, and the residue, by "instalments within six months thereafter, the directors "being authorized to sell the shares of any stockholder who "may be delinquent in paying his instalment. Section 5205 "provides that every association which shall have failed to "pay up its capital stock, as required by law, and every as- "sociation whose capital stock shall have become impaired "by losses or otherwise, shall within three months after re-

"ceiving notice thereof from the Comptroller of the Cur-
"rency pay the deficiency in the capital stock by assessment
"upon the shareholders, and if this is not done within the
"time limited the association must go into liquidation, or
"a receiver be appointed. With the greatest care and pru-
"dence it is not possible always to avoid losses, which may
"be so large as to sweep away part of the capital, but by
"the provisions of the section last-quoted and a system of
"reports and examinations designed to disclose the true
"condition of the bank to the officials of the Treasury De-
"partment, Congress sought to minimize the results of such
"misfortune by requiring the bank promptly to make good
"its depleted fund or to cease doing business. It may be
"noted that the payment of assessment under Sec. 5205 to
"make good impaired capital and so enable the bank to
"continue doing business does not relieve the shareholder
"from the double liability of Sec. 5151. But the capital of
"a bank may be depleted otherwise than by losses; it may
"be distributed in the form of dividends to the shareholders.
"To this method of depletion of the fund known as 'cap-
"ital,' Congress opposed the prohibition of Section 5204:
"'No association, or any member thereof, shall, during
"'the time it shall continue its banking operations, with-
"'draw, or permit to be withdrawn, either in the form of
"'dividends or otherwise, any portion of its capital.'
"Nothing is said as to 'intent'; the sentence is a flat
"prohibition of the act of withdrawal. The language in
"which this prohibition is cast is the most drastic used in
"the whole Title. In one section (5209) certain acts are
"declared misdemeanors when done by 'president, di-
"'rector, cashier, teller, clerk or agent of such associa-
"'tion'; in another section (5208) it is declared unlawful
"for 'any officer, clerk or agent' to do certain acts; in
"still another section (5207) 'any association offending
"'against the provisions' of the section is declared guilty

"of a misdemeanor and fined, and 'the officer or officers' "so offending are required to pay an additional fine. In "most of the sections containing a prohibition the language "used is 'no association shall'; a form of words which lays "the inhibition solely upon the association or its officers "and does not personally disqualify the persons dealing "with the association or with such officer. Thompson *v.* "St. Nicholas National Bank, 146 U. S. 251.

"But by section 5204 Congress has reached over and "beyond the association and its officers and has laid upon "the individual shareholder (although not a director, or in "a position to know the bank's condition) a prohibition as "peremptory and unqualified as that laid upon the bank "itself. '*No* association, or any *member thereof*, *shall* "'*during the time it shall continue its banking opera-* "'*tions*, *withdraw*, or permit to be withdrawn, either *in* "'*the form of dividends* or otherwise, *any part of its* "'*capital stock.*' The use of this particular form of "words is most suggestive, and the language used is cer- "tainly unambiguous. When the defendants, therefore, "received these dividends out of capital, they withdrew the "moneys so received, from the special fund which under "the statute was to be created and preserved intact as a "reserve to secure those dealing with the association against "loss in the event of failure; and they did this when the "statute expressly forbade *them* to do so. They have "depleted the fund which it was made *their* duty (as "well as that of the officers and directors) not to deplete: "they have received money belonging to the bank to which "they had no right and for which they have given no con- "sideration, and since that money was pledged for a specific "purpose, viz: the maintenance of the capital intact as a "fund for the protection of depositors and other creditors, "future as well as present, its diversion into the hands of "defendants was a fraud upon those for whose benefit such

"fund was created. The bank would have had as good a "right to recover from its shareholder money thus received "without consideration, as it would to recover from its "president for overpayments of salary, and to that right of "action the Receiver has succeeded. It is argued that by "such a construction of Sec. 5204 the stockholder in a "national bank is exposed to great hardship; that he may "go on for years receiving dividends, ignorant of the mal-"versations of the bank's officers, of the supine negligence "of its board of directors, of the incompetency or careless-"ness of the examiner, and then suddenly find himself "called upon to repay what he honestly supposed he was "entitled to. That seems not to be a sufficient reason for "construing the section otherwise than in conformity to its "express terms. The hardship imposed is no greater than "is that imposed by the double liability section (5151). "Congress was apparently concerned with the question of "security to those dealing with the bank, rather than with "the hardships which might result to the shareholders "who were so unfortunate as to confide the conduct of their "bank to officers and directors who might turn out to be "incompetent or dishonest."

The above is taken from Judge Lacombe's opinion. All the sections to which he refers are printed in full above.

Section 5204 which provides, as above said by Judge Lacombe, that—"No association, or any member thereof, "shall, during the time it shall continue its banking "operations, withdraw, or permit to be withdrawn, either "in the form of dividends or otherwise, any portion of "its capital," makes a dividend paid out of capital *ultra vires*, not of the board of directors merely, *but of the whole association*,—

California Bank v. *Kennedy*, 167 U. S. 362, and makes it also *illegal*.

Trevor v. *Whitworth*, 12 App. Cas. 409.

II. *The making of the dividends being both* ultra vires *of the association and illegal and the* taking *of them being illegal also, they can be recovered back.*

The money was always and still is the property of the association and the defendants have not the slightest interest in it. As was said in *Bartlett* v. *Drew*, 57 N. Y., 587, already cited: (p. 590) "As before suggested it does "not matter how it came to the possession of the defend- "ant Drew. *It is enough that he had it.*"

There are numerous cases upon this subject in England arising under the Companies' Act. They vary a good deal, because the powers of a company under the Companies' Act are defined, not by the act, but by the "memorandum of association," but they are uniform in this—that a dividend made out of capital is *ultra vires* and "invalid" and can be recovered back.

They differ as to what *is* "capital."

In *Stringer's Case*, LR4Ch475 (1869), both of the Lords Justices of the court of appeal said that a dividend paid out of capital would be ordered to be paid back in the winding up (pp. 489, 494). In that case however the court held that the dividend had *not* been paid out of capital.

Holmes v. *Newcastle-upon-Tyne Abattoir Company*, 1ChD628 (1875). In this case a shareholder compelled the other shareholders to repay their dividends *to the company, it being a solvent and going concern.*

Guinness v. *Land Corporation of Ireland*, 22ChD 349 (1882), where Mr. Justice Chitty after quoting Lord Hatherly's judgment in *Macdougall* v. *Jersey Imperial Hotel Company*, 2 H. & M., 528, 535, said: (p. 361.) "That second proposition appears to involve this, that if "the dividends are paid out of capital to the shareholders, "in the winding up *the persons who receive it* would be "liable to repay. That portion of the judgment was cited "with approval by Mr. Justice Fry in the case of *In re*

" *Alexandra Palace Company*, 21 Ch. D., 149, where he " says that in his view what I have just read lays down " the law with perfect precision, and he goes on to say " (*Ibid.* 160), 'I think no subterfuge by which it is at- " 'tempted to return capital to shareholders, and thereby " 'to diminish their liability, ought to be countenanced " 'for one moment by this Court.'"

In the same case on appeal the Lord Justice Cotton said: 22ChD375. "In my opinion it also follows " that what is described in the memorandum as the " capital cannot be diverted from the objects of the society. " It is, of course, liable to be spent or lost in carrying on " the business of the company, *but no part of it can* " *be returned to a member so as to take away from the* " *fund to which the creditors have a right to look as that* " *out of which they are to be paid. In former days pro-* " *ceedings could be taken against members of a com-* " *pany*, but under the present law a creditor has no rem- " edy except execution against the goods of the company, " or winding-up proceedings. If a winding-up order is " made *each shareholder is liable to contribute* the amount " not paid upon his shares, including *what if anything he* " *has had returned.*" And also the judgment of the Lord Justice Bowen (p. 380).

Gooch v. *London Banking Association*, 32ChD41,47.

In re Oxford Benefit Building and Investment Society, 35ChD502. In this case the directors were held liable for paying dividends out of capital, with a reservation of their rights to recover from the shareholders. (p. 517).

See *In re Sharpe*, [1892] 1Ch154.

Ooregum Gold Mining Company v. *Roper*[1892]AC125.

The language of Lord Herschell, in *Trevor* v. *Whitworth*, 12 App. Cas. 409—where he says at p. 415 " what is the " meaning of the distinction thus drawn between a com- " pany without limit on the liability of its members and

" a company where the liability is limited, *but*, in the " latter case *to assure to those dealing with the company* " *that the whole of the subscribed capital*, unless dimin- " ished by expenditure upon the objects defined by the " memorandum, *shall remain available for the discharge* " *of its liabilities?* The capital may, no doubt be dimin- " ished by expenditure upon and reasonably incidental " to all the objects specified. A part of it may be lost in " carrying on the business operations authorised. Of this " all persons trusting the company are aware, and take " the risk. *But I think they have a right to rely, and* " *were intended by the Legislature to have a right to* " *rely, on the capital remaining undiminished* by any " expenditure outside these limits, or *by the return of* " *any part of it to the shareholders.*"

Italics mine.

runs through all the later cases.

Of the cases cited by the defendant's counsel *Stringer's Case*, LR4Ch175 has already been referred to.

In *Rance's Case*, LR6Ch104 a director was ordered to repay a dividend which had been paid to him out of capital. It did not appear that the company was then insolvent.

Re Denham 25ChD752, if it turns on other than section 165 of the Companies Act, 1862, is contrary to Mr. Justice Chitty's later decision in *Guinness* vs. *Land Corporation of Ireland*, 22ChD349, already quoted.

The argument is pressed that it is a great hardship to make a stockholder pay back dividends which he received in the belief that they had been earned. But it would be a greater hardship upon the creditor to let the stockholder keep them. The stockholder can examine the bank when ever he pleases. If he finds the directors are paying divi-

dends out of capital, he can vote them out, or if he cannot get enough other stockholders to join with him he can apply to the comptroller of the currency. He need not take his dividend until he has ascertained these things. What is more, the stockholders originally chose those who have made the dividends out of capital.

The creditor has no such rights, and, he had no voice in the choice of the managers. All he can do is to rely upon the statute that the stockholder shall not "withdraw," "either in the form of dividends or other-"wise, any portion of its capital."

III.

Equity has jurisdiction.

In *Finn* v. *Brown*, 142 U. S. 56, a judgment at law upon a verdict was sustained by the Court, but the question was not raised and was therefore waived.

On the other hand in *Vose* v. *Grant*, 15 Mass. 505, the court, after saying (p. 521) that the creditors ought to be paid out of the funds which the stockholders had with drawn from the bank, held that it could not be effected at law, and, as the Supreme Judicial Court of Massachusetts had no equity powers, it could give no relief: Mr. Justice Jackson saying (p. 522): "*This is one of the numerous cases, which are constantly occurring, which show the necessity of a court of chancery for the complete distribution of justice among the people.*

Italics in the original.

Mr. Justice Story, in his treatise on Equity Jurisprudence, following what has been already quoted, viz.: "And if the capital stock should be divided, leaving any "debts unpaid, every stockholder receiving his share of

" the capital stock would in equity be held liable *pro* " *rata* to contribute to the discharge of such debts out of " the fund in his hands," said (§ 1252): " *This, however,* " *is a remedy which can be obtained in equity only;* for " a Court of Common Law is incapable of administering " any just relief, since it has no power of bringing all the " proper parties before the court, or of ascertaining the " full amount of the debts, the mode of contribution, the " number of the contributors, or the cross equities, and " liabilities which may be absolutely required for a proper " adjustment of all parties as well as of the creditors."

1. *Of course if it be decided that the capital was a trust fund for the creditors, the jurisdiction of equity is undoubted.*

As already quoted, *Curran* v. *Arkansas*, 15 How. 304, *the Court said:* (p. 307.) " If they have been " distributed among stockholders or gone into the hands " of other than *bona fide* creditors or purchasers, leav- " ing debts of the corporation unpaid, such holders " take the property charged with the trust in favor " of creditors, *which a court of equity will enforce*, and " compel the application of their property to the satis- " faction of their debts."

2. *But suppose the other sort of case, that, under the Acts of Congress, the distribution of the money by dividend has been* ultra vires *and illegal.*

In that case also equity has jurisdiction, because, even in that case, the action being brought, as this one is, for the final winding up of the affairs of the bank—the stockholder is entitled to all the remainder of the assets after the debts are paid, and he is therefore entitled to *keep*, as against an action by the receiver, *so much of what he has received as is not necessary for the payment of the debts.* And it follows that a bill lies for a contribution against all

the stockholders, that being the sort of a case in which the solvent stockholders can be made to make up for the shares of those who turn out to be insolvent.

It is well settled in the practice of the equity courts of the United States that, owing to the imperfection of the jurisdiction over the parties, a bill for contribution is properly filed, if filed against all the parties in the jurisdiction, although there may be others, and the most of them, out of the jurisdiction; this, of course, being the sort of case where the parties out of the jurisdiction, though "necessary" in the sense in which that word is ordinarily used, are not "indispensable," as an owner of the equity of redemption in the foreclosure of a mortgage or a part owner of the land in a partition. *Coillon* v. *Millaudon*, 19 How. 113, 115; *Barney* v. *Baltimore*, 6 Wall. 280; *Swan Land & Cattle Co.* v. *Frank*, 148 U. S. 603, 611.

That it happens to turn out in this case that *all* the money paid as dividends is needed, cannot alter the jurisdiction. *Homer* v. *Henning*, 93 U. S., *Stone* v. *Chisolm*, 113 U. S., 302; *Ogilvie* v. *Knox Insurance Co.*, 22 How., 380; *Swan Land and Cattle Co.* v. *Frank*, 148 U. S., 603.

3. *But the question certified is not confined to dividends paid out of capital. It includes dividends made when* insolvent.

The question is—"Has a U. S. Circuit Court jurisdic-
"tion to entertain a bill in equity brought by the receiver
"of a national bank against stockholders *to recover divi-*
"*dends which it is claimed were improperly paid* when
"such suit is brought against two or more stockholders
"and embraces two or more dividends, and when the ob-
"jection that there is an adequate remedy at law is raised
"by the answer?" (R. 3.)

The question is therefore whether equity has jurisdiction of a bill for dividends declared and paid when the bank was *insolvent*.

This is answered by *Curran* v. *Arkansas*, 15 How, 304, and the other cases adjudged by the Court cited above—and so are all the English cases. It is true, that the most of these latter are winding-up cases, which go to the Court of Chancery by statute; but all the other cases are in equity also.

We submit that there are in the books but three cases at law brought to recover dividends.

The first is *Finn* v. *Brown*, 142 U. S. 56, where the question was not raised.

The others are the two Massachusetts cases, *Vose* v. *Grant*, 15 Mass., 505, and *Spear* v. *Grant*, 16 Mass., 9—in each of which the plaintiff was beaten because the action was brought at law, and not in equity.

Both questions should be answered in the affirmative.

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